ONTARIO

P R O C E E D I N G S

OF THE

SELECT COMMITTEE APPOINTED BY THE LEGISLATURE OF THE PROVINCE OF ONTARIO, TO ENQUIRE INTO AND REPORT UPON MATTER IN CONNECTION WITH TOLL ROADS IN THE PROVINCE.

Mr. J. P. Robarts, Q.C., Chairman,
Presiding.

Mr. D. J. Collins, Secretary.

VOLUME IV

Wednesday, October 19th, 1955.

New York City, N.Y., (U.S.A.)

R. C. Sturgeon,
Official Reporter,
Parliament Buildings,
Toronto, Ontario.

F O U R T H   D A Y

New York City, N.Y.,
Wednesday, October 19th, 1955,
10:00 o'clock, a.m.

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The further proceedings of this Committee reconvened pursuant to adjournment.

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PRESENT:

Mr. J. B. Robarts, Q.C., Chairman, Presiding.

Messrs. Yaremko, Q.C.,
Root,
Sandercock,
Mackenzie,
Jolley,
Auld,
Manley,
MacDonald,

Mr. D. J. Collins, Secretary.

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APPEARANCES:

Mr. W. J. Fulton,	Director of Planning, Ontario Department of Highways.
Mr. W. Q. Macnee,	Traffic Engineer, Ontario Department of Highways.

Mr. Donald MacFadden, (Partner) Mr. John Power, (Partner) Mr. Graham Lynch, Mr. Lloyd Gelmour, (Senior Partner) Mr. S. Logan Sterling, Mr. D. F. Barton, Mr. H. L. Bogert, Mr. John Ellis, Mr. J. B. Callum, Mr. John Carleton,	Partners in and representatives of Messrs. Eastman, Dillon and Company.
Mr. George Jamieson,	Representing Wills, Bickle Company.
Mr. James Skelley, Mr. David Weldon	Representing the Midland Securities Corporation.

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MR. WELDON: Gentlemen, shall I "kick it off" and introduce Mr. Donald MacFadden, who is the head of the Eastman, Dillon Company's Revenue Bond Department, and perhaps one of the leading authorities on the financial aspects of toll roads in the United States.

Just to comment on that; they showed me some figures last year, and I think the total financing of toll roads in the United States is something like five billion dollars, and to date, the Eastman, Dillon

firm has participated in a little over 90 percent. of that, so Mr. MacFadden is well qualified to discuss these aspects of toll roads with you. If it is agreeable to you, may I ask Mr. MacFadden to take over the meeting and lead the discussion.

MR. MacFADDEN: Thank you, very much. I want to thank our good Canadian friends, Mr. Skelley and Mr. Weldon, of the Midland Securities Corporation, and Mr. Jamieson of Wills, Bickle, for making this meeting possible.

We appreciate your presence here, and I hope our meeting will be profitable to you.

We are going to be here and at your disposal for any type of questions you wish to shoot at us.

I thought perhaps it would be helpful if I outlined briefly the various steps a toll road takes from the first desirability of issuing bonds, through the various problems, up to the point of marketing. I think this will make possible a general picture, and bring into light the kind of questions you may care to ask, and which perhaps will answer some, and may suggest others.

If that is agreeable, Mr. Robarts, I will proceed along that line.

THE CHAIRMAN: I think that will be very

helpful.

MR. MacFADDEN: A toll road, like any undertaking, is an economic enterprise, and can be justified only from the standpoint of what it will do, and those can usually be defined as the time saved by travelling on a toll road and the distance saved in between the terminal points on the road, and between the intermediate points, and the cities which are served enroute.

The justification of savings in economic terms naturally hinges basically and particularly upon these two terms, and, of course, over and beyond that is the factor of convenience and aiding the public, and thereafter, the very important factor of safety of travel. That, as you know, has become more and more important as our accident rates mount, and the traffic on our congested roads continues to increase.

With these factors in mind, the route and alignment of the road becomes very important, in order to serve and induce or attract the maximum traffic the road can draw unto itself.

The route selection really is the joint responsibility between the traffic engineer, who must lay out the road, in the sense of where it will go to draw the maximum amount of travel, and the civil engineers, who, on the other hand, must lay it out in physical terms

of grades and economy of construction. So the route selection is really a joint responsibility of those two people.

Those are some of the points which justify a toll road, and really determine the extent of its advantages. The advantages to a state or province, as you well know, naturally lies in the creation of many traffic arteries, which will be paid for directly from revenue derived from them, and the corollary of freeing those funds for the further development of your secondary road system, and keeping the over-all tax load at the lowest levels possible. I think those are all very obvious answers.

In approaching the financing of a toll road, the first thing which must be established, naturally, is its feasibility. Can it pay its way? Is it immediately necessary? And in that regard, there is just one accepted approach, and that is the engaging of engineering people to make those basic studies, as you must have a traffic engineer who can estimate the traffic which will be carried, if it is drawn to the road.

On the other hand, you must have a construction engineer's study, which will give you the cost factor involved.

From these two studies, the adequacy of revenue is determined, and hence the margin of safety above the operating and necessary maintenance costs which will accrue to the bond issue, and create the margin of safety which the investor not only requires but really demands.

The acceptability of debt coverage on our various roads is found from experience, too, and is, to a very real degree, governed by the locality and region through which the road passes.

I think you can readily understand from some of your recent trips that a road which goes through a heavily-congested traffic area, such as New Jersey, and points along the Atlantic seaboard, will have a public acceptance, but a road built in Iowa or Kansas may be considered questionable.

The need here is so great that it cannot always be interpreted in fringe areas in terms to the same degree of economic need, and I think in your area in Canada -- and this is merely conjecture -- you will find you will need certain education on your traffic problems and on other different needs. They can well be established through your engineering surveys.

Looking at the map, and not knowing but very little of what you have contemplated, I would say the

ingredients are present, and the need could be very real for such a project in your province.

In regard to the coverage of the bond: as I have indicated, the margin of safety is affected by the rate of interest they have to carry, and on the bond issue, as I imagine may be comtemplated here, I think it is apparent you will have to come -- and most probably will come -- to the United States market, at least for a substantial part of the funds, and in that sense I think it is well to realize that a revenue bond of Canada in the United States is without one important protection our domestic rates have, and that is, Federal tax exemption, so those bonds to an investor would have rather a limited appeal.

So your first and necessary thing would be to tailor such bonds for institutional acceptance. By that I mean our larger and intermediate association of insurance companies, fund foundations, and that sort of investment reservoir of funds. In the very final analysis, they will not only dictate the terms of the safety factors of your bonds, but they will dictate them in such a manner that if they do not find them acceptable, you will simply have not a market for your bonds.

Let us presume for a moment that you find --

as a number of roads in this country have found from basic engineering -- that the coverage which may come down to the bonds is sort of border-line.

In that case, we have found from experience, that it has worked out very favourably in a number of cases, but other things may be injected into the bonds which may enhance and bring the security flow up to a substantial level and again, without knowing either the philosophy of your picture up north, or what you may have in mind, several things occur to me which could help a bond in Canada, based on revenue, if it approached a border-line situation on a revenue basis.

Amongst these -- and you have had experience with a number of things -- the provincial guarantee would be one thing. You have had that successfully, and over a long time, on The Ontario Hydro-Electric Project, and one or two other things.

It is also possible that the province might agree to assume the guarantee of a deficit, should a deficit arise from operations.

Those are the two things which immediately come to mind. They may be politically inexpedient; they may be undesirable to contemplate. But those are the two important thoughts.

Beyond that, there are alternatives. We have

found it, and it has again been worked successfully. That situation needs a further build-up in securities, and in certain cases the State Highway Departments have stepped forward and assumed, let us say, their portion of all the normal operating and maintenance expenses. That, in fact, has made the bonds a first lien on the gross revenue of the project, and that often is a step which is useful in building up the security under a bond.

Another alternative could include -- as we have done here -- an allocation of certain taxes, that is, the apportionment of a portion of the taxes to support these bonds. And I add again, these things might be employed if necessary, and to the extent necessary, and the greater security you can breed into the bonds, the more assured your chances of successful fund raising would be.

I understand in this case, your road is partially built, that some of it is laid out, and rights-of-way have been acquired. That lends itself to another thought which might, to a degree, be called "subsidization" and if you needed to build any greater security, it might be possible that certain portions of the road which have already been paid for by the province, might be, in a sense, contributed to this toll-road project, which

would naturally cut down the requirements, and the cost of financing, and increase again the security of your bonds.

I think there are a number of other approaches to this question, which could be developed, and without more than a very, very general knowledge of what you have in mind, we are naturally handicapped in going much further.

These factors of assistance could be developed, but to what extent they are developed will depend very largely upon the feelings of the bankers you may ultimately choose to work with, to prepare these for marketing, or upon the financial people with whom you may choose to work during the building-up stages.

In this connection, I might point out there are but two really acceptable means of toll-road financing, which have been accomplished in this country to date.

It includes, first, the engaging of a fiscal agent, so-called, whose duty it is to see that the ground work of preparing the entire bond indenture cf all of the attendant instruments and papers, and bring the issue up to a point where it is then ready to market. Such a fiscal agent is usually employed on a contract basis -- on a fee basis -- for that sort of

undertaking for a substantial issue, the fee is usually quite substantial.

The other method which is of greater advantage to an issuing body, as you may represent at some future time, is really the appointment of bankers, a banking and management group.

At this point -- whether it is a fiscal agent or bankers to build up this type of business -- you would draw on the same people, the same investment banking houses, which might be qualified to set this up, just as a fiscal agent would be the same people -- qualified bankers,-- to be appointed to do this work.

The advantage to you, as the issuing body, would be that through the appointment of bankers, or a banking and management group, you will receive the same services, and probably a more directly and avidly-interested service, from the bankers than I think you would from the fiscal agent. The reason is simply that the banker is working without fee, while doing all of the things which the fiscal agent would do for a fee, and it is only through him having the time and putting in the efforts, and the money spent through his efforts, which assures the ultimate and successful consummation of the financing. He then, through the normal proceeds of any financial operations, is

rewarded for the services he has given in building this up to a point of marketability.

Those two are the only accepted means we have found in this country for that type of financing.

I would add to that, that whether a fiscal agent or bankers in this connection, I would urge they be selected very early in your programme, and a great many costly mistakes can be so avoided. A number of important firms have had great experience, and all I have to say is that they have stubbed their toes, and stubbed them badly, in gaining that experience.

That experience is available to you people who are going into this deal for the first time, and I think you should avail yourselves of it early in your programme, and bring them along with you, and as your programme unfolds, they can help you a great deal.

The work of either the fiscal agent or the banker enters into your picture at an early date, from the point of view of your engineers who make the basic surveys. You will find they are working with him, and watching him like a hawk, in co-relation with the work of the two engineering groups, and also in conjunction with you, if you may, at that time, be representing the issuing body, as an Authority.

Then, too, they will go through all of the

steps necessary for the presentation of the indentures, and they will tell you of the pitfalls which you may encounter. Theywill tell you what must happen to every penny and nickle in connection with your highway situation, and, finally, advise on the preparation of a prospectus, which is the vehicle through which the bonds must ultimately be sold.

These essential steps being taken, your bonds then approach the point of being marketed. If you have started off with a fiscal agent, you must, in most cases, at that point, so-to-speak, switch horses, as the fiscal agent normally can go no further.

Then you must appoint a banking group, which will be qualified to underwrite the bonds. There again, another advantage arises. If you change horses at that point, you do not have the advantage from a banker thus appointed, that you have with a banking group appointed in the early stages, which knows the problems, and has lived through them, and has a greater degree of familiarity than someone entering the picture later can ever gain.

But, regardless of how you arrive at that point, your banking group will put together a syndicate to underwrite the bonds, and if it is an issue of $100 million or more, the syndicate would comprise

200 or 300 -- or maybe more -- investment firms scattered throughout this county and throughout your own.

Coincidentally, at that stage, the institutions throughout the country must be approached, and usually the large ones are approached on a very direct and personal basis, and an educational basis, in this instance, where you are pioneering in the sense that there has never been a toll-road issue which has been brought to market, which has carried taxable coupons, and also there never has been, as you know, in your country. So, in a sense, you are pioneering, and you will have the extra impediment which has to be overcome of selling a new vehicle, with new attendant factors to the institutional buyers who will control the successful accomplishment of your underwriting.

I would like to stress once more the importance of your group of bankers who will be selected to do this ultimate financing. There are any number of good banking firms in this country, and in your own, but, by all means, when you reach that point, be sure you select from amongst the best, because their selection in itself, will give your bond issue a certain standing not only in the investment field, but in the field of the ultimate purchasers; it will carry weight with the

institutions, and which, as you are aware by now, will bring to you the experience and knowledge which has been rather hard gained in this field.

Another point I think is well worth keeping in mind is that whoever you choose in this deal, you will be living with, and living with them pretty closely. There will be a number of difficulties -- not animosities -- but difficult problems to solve, and I think you must have, not only someone in which you have complete confidence, but should choose someone with whom you feel you can live, and live with comfortably during some of these difficult times in your major financing experience.

In regard to the types of financing; there are only two methods we have used in this country. One is what you might call the "private placements" that is, placement of bonds without a public offering, direct to a relatively small group of major institutions.

There is no distinct advantage in that, but it brings about a saving to the issuing body, in that under those conditions, the funds are taken down from the ultimate investor only when they are needed, and as construction progresses.

That, frankly, is a very difficult way of

doing it, and there has only been one successful accomplishment in this country, and that was the initial New Jersey Turnpike.

In support of that point, I might say that there have to date in this country been sold, $4,318,000,000 of toll-road bonds, and of that entire total, only $222,000,000 -- that was all one issue -- have been successfully placed privately.

I might mention at this point -- as Mr. Weldon mentioned earlier -- that we take a pardonable pride in the fact that out of that total toll-road financing in this country of $4,318,000,000, we have been either a principal participant or manager in 93 percent. of that total.

While the private placement is difficult to accomplish, it most certainly must be explored, and, in that eventuality, I think you will find you will come to the public market with securities.

Other factors upon which I may touch very lightly and which you may be thinking of, are, first, the employment of a traffic engineer and a civil engineer to make the preliminary studies, you will have to have a source of funds for their employment. You will perhaps need legislative enactment for that.

I do not suppose you have as yet created a

toll road Authority.

THE CHAIRMAN: We are exploring it, only.

MR. MacFADDEN: In that regard, both in your country and perhaps in ours more than yours, at this point there are attorneys who have made a career -- there certainly has been the greater part of their time spent in that direction -- and these attorneys could be of great value, as well as a banker might be of value, in preparing the basic legislation, which will meet all of the possible exigencies which might arise.

I think that is an important point, because altogether too often we have found legislation enacted to accomplish a purpose like this, and somewhere along the line a cog has slipped, and new legislation, remedial in nature, has had to be brought into the picture.

I think, in matters of a specific nature, this agency could accomplish things which would be helpful during the primary promotional stage.

I would like to turn this into an open forum, and if you will shoot at us questions, from any direction, concerning things you may have in mind, we will try our best to come up with the answers.

MR. WELDON: You mentioned the employment of

outside engineers: It would not be out of line to use the knowledge of the personnel in your department?

MR. MacFADDEN: Frankly, I think your present departmental engineers are at least equal to any engineer you might hire from the outside, but, regardless of that, the investment market will demand and require an independent engineer, and they, in turn, you will find, will always work very closely with, and draw some of their information from, your personnel in the Highways Department, but the name on the report of an independant concern is a "must".

MR. MacDONALD: How serious a factor is this taxing of bonds in Canada, in terms of floating a bond issue?

MR. MacFADDEN: I think your question really boils down to this; since your bonds have no tax exemption as in this State, probably a higher rate would be necessary to carry out the saleability down here.

MR. MacDONALD: That is right. I agree with you.

MR. MacFADDEN: This is simply a case: for example, next week the Illinois Turnpike Commission will sell $400,000,000 worth of bonds for the Turnpike system, surrounding and emanating from Chicago, and I would expect they would carry a rate of around 3-5/8 percent.

to 3-3/4 percent., the higher rate because of its size than would be applicable on a small amount. I think with straight bonds, you have to add 1 percent. to that.

Do not take that too seriously in this sense, that the higher rate of interest may cause discussion on the home front within your province; it may seem like a high rate, but the higher rate of interest has a particular influence on the bond coverage.

The difference between 3-3/4 percent. and 4-1/2 percent. or 4-3/4 percent. increases the debt load, but is not as burdensome as you might figure.

MR. COLLINS (Secretary): Do the Illinois bonds have state backing?

MR. MacFADDEN: Very few of our Turnpike bonds have state backing. The Illinois bonds are under the Authority created under a state law, but they have no reference to the credit of the state.

Where the state credit has been placed behind or loaned to the toll road undertaking -- as happened here in part, and part of the New York Thruway bonds, and in Connecticut -- it naturally means a lower rate of interest, because the ultimate security is the security of the state.

MR. COLLINS (Secretary): Would it be 1 percent.

lower?

MR. MacFADDEN: I would say roughly 1 percent. might be usual.

THE CHAIRMAN: What type of administrative organization for a toll road project is considered most favourable, from the investment point of view?

MR. MacFADDEN: You mean as the issuing vehicle?

THE CHAIRMAN: No, the actual operation and construction of your facilities. Do you use a Commission? Are the people interested in how they are appointed, and who they are?

MR. MacFADDEN: One would understand that it is important they be capable people -- good people. How they are appointed is not within our realm.

THE CHAIRMAN: I was wondering if any of the facilities you have underwritten as a toll road, have been operated by some branch of state government as opposed to an independent toll Authority?

MR. MacFADDEN: I cannot think of a single instance, unless it might be a very short toll road in Colorado, between Denver and Boulder, but I am not certain of that.

The answer would be in almost all cases that it would be operated by a separate Commission or "Authority" as we call it. As it has developed here,

a body appointed by the Governor or a Legislative group -- a representative group -- numbers usually from six to nine or ten men of good calibre and sound experience, who form the administrative body.

They, in turn, will engage and develop an administrative staff which will really run the road, and all the factors other than the development stages, but certainly through its operating period.

One other thing which was not mentioned -- although at this point and juncture, I do not think it is too important, but which is going to be a factor in connection with the desirability attached to the bonds, will come from certain technical information like the call feature attached. However, I think that is in the future, and can be worked out.

MR. YAREMKO, Q.C.: Can you give us an idea of the cost of these original surveys which have been made?

MR. MacFADDEN: In the first place, I do not know very well the extent of the operations you have in mind, whether it is a 50-mile undertaking, or what it is, but I understand some work has been done on both the alignment, and even on some of your grade work.

If you were thinking in terms of, let us assume, 100 miles of road, upon which nothing has yet been done --

and this is purely a guess; I would not want to be held to it in any sense -- I think a traffic report might cost, under this Committee, in the neighborhood of $35,000.

Your construction report would be perhaps from two to two and one-half times that much. I hesitate to inject that at this time.

Graham (Mr. Lynch), can you add anything to that?

MR. LYNCH: The only thing which I could add is how efficient would be the construction, since you have a good deal of engineering already in progress. The outside engineer would probably not vary it very much, because it would have to be done from the beginning over the entire project.

What you have done so far would not really help a traffic study. I would say that $35,000, or maybe a little higher.

MR. MacFADDEN: And your civil engineer, with the necessity of aligning, and borings, and that sort of thing, might run from two to two and one-half times that.

MR.LYNCH: Yes. So much has been done, it might be cut down a bit in your case.

MR. Mac FADDEN: In discussions on that point,

I think you will find, as you go into this field, you must be very careful in the selection of your engineers. Certain engineers carry more weight with the investing public, and are more readily acceptable, because the bonds, to a large degree, are bought on the experience, record and wisdom which put the project together.

MR. SKELLEY: I think you mentioned there were only three firms who were qualified in New York?

MR. MacFADDEN: Cloverdale and Colpitt, Parson and Brinkohoff, Hill and MacDonald, and Wilbur Smith and Associates.

There is one more which has done considerable work, and that is Delieuw and Cather, of Chicago.

MR. LYNCH: And there is another one, Madigan and Hyland.

MR. MacFADDEN: They do so much work for New York, as I know from personal approach, that they have no time for anything else.

MR. LYNCH: Delieuw and Cather are specialists in civil engineering.

MR. MacFADDEN: In talking with Mr. Delieuw, I learned they might swing back to the traffic field. They have done good work, but they swung away from it for awhile.

MR. FULTON: They are working for us now.

MR. MacFADDEN: And they are good people. "Charlie" Delieuw stopped in one day last week, and he was leaving for Turkey, and he was going to lay out a road in Turkey, and he engaged Messrs. Gruner and Company to estimate what it would cost, and whether it would be feasible to build a bridge over the Bosporus.

He thought they might have to round up the entire traffic in the country and run it across the bridge. That country apparently is looking forward to future needs.

MR. MacDONALD: From the investment point of view, what is the attitude toward the government backing the bonds? Do they regard it with favour?

MR. MacFADDEN: They could, unquestionably.

MR. MacDONALD: Is there any feeling that it draws politics into it, which may be disadvantageous?

MR. MacFADDEN: No. There are politics on every level, but that is all relative. It is a practical thing in life, as we live it. I do not think it casts any shadows at all, unless there might be an area where politics were virulent, and extremely bad. That has happened in one or two of our states in times past, to the harm of the states' credit. It

would be harmful, but from the point of view of bond security, it would be the strongest thing you could bring into it.

Judging from other states, there may be a strong desire not to use the credit of the state or province. They would rather save it for other things where it is mandatory. If an undertaking of this sort can be done on its own, or with an element of assistance perhaps through the allocation of taxes, it would be an indirect assist, without involving the credit of the state.

MR. LYNCH: In that respect, I might point out that where the state guarantee has been used, it has been used to aid a project on the border line.

The New York Thruway, for instance, realized if it was a straight revenue bond, payable solely from the tolls of the project, the project could not have been done, so the state guarantee was necessary for a portion of it.

The New Jersey Highway Authority is another example where the state guarantee was used. That project would not have been feasible on their own, and it was necessary to bring the state guarantee into it.

Where it is not necessary, I cannot think of a project which does have the state guarantee at this

time.

MR. MacFADDEN: There is one corollary benefit -- I think it was in the State of Connecticut -- where the state credit was behind a system which consisted of the beneficial toll road.

MR. LYNCH: In the case of Connecticut, it has the credit of the state supporting it, but it is still not a state guarantee.

MR. MacFADDEN: That is correct. That is not a state guarantee.

MR. LYNCH: And the credit would add to the security by pledging a portion of the gasoline revenue and so forth.

MR. POWER: Did they guarantee the deficit by the state?

MR. MacFADDEN: I wonder, Mr. Robarts, -- I understand this is essentially a fact-finding group, but I wonder if you might want to say something as to how you see your plans, or what you might be looking for, which may enable us to bring this discussion more directly into helpful lines.

THE CHAIRMAN: I thought we might have made this clear before.

We are a Committee appointed by the Legislature of Ontario to investigate and bring back recommendations.

Whether our government will accept or reject those recommendations , we do not know. They do not need to accept them, of course.

We are doing exploratory work -- I think it would be fair to say -- in the purest sense of the term.

We were very much interested in meeting with you this morning, and discussing this, and seeing how it is being done in other jurisdictions. Whether it will ever reach that point in our province, we do not know, and I do not think we have reached the stage where anybody can forecast as far as the government is concerned.

Therefore, we are having a very theoretical discussion, from our point of view, this morning. I think I should make that clear. We are interested, actually, in everything and anything you can tell us.

I was going to ask you if you could give us any information regarding the State of California. I understand they have a very large construction programme under way, but no tolls whatsoever, and yet they have financed that in the public-money market.

MR. MacFADDEN: California has been a state, in its highway programme, which has politically been dedicated to the freeway, and the development of the

free highway system.

They have flirted once or twice in recent years with the toll road idea, but thus far they have not deviated from their political philosophy.

As a result, the bonds are supported by taxes from all sources in their payments.

At some future time, they may deviate from that, but that has been their philosophy to date, and they have adhered to it.

THE CHAIRMAN: This may be out of your field slightly, but have you any idea why they adopted that attitude? It is very interesting for us to find this one state with a very tremendous problem doing it differently from some of the other states.

MR. LYNCH: In that respect, you might say that California is a high-spending state. It is a very wealthy state, and they could issue bonds for road purposes without injuring the credit of the state too severely.

Their credit has been dropped to a double "A" rating, simply because of the outstanding debt, which is piling up in California.

They are not completely adverse to the revenue bond type of financing. Practically all of the major bridges carry revenue bonds. The Toll Bridge

Authority, which has built the largest bridge in the state of California, was built by revenue bond financing.

MR. MacFADDEN: I say this without any inside knowledge, but from all outward appearances, it is political philosophy to date, which may or may not be altered at some future time, through expediency. If the state finds its highway demands are greater than it can support without state credit, it will undoubtedly move into the toll road field.

MR. MacDONALD: Again, from an investment point of view, is there any feeling of preference for bond issues, revenue bonds or revenue directly from the road being dedicated to a kind of free-road system?

MR. MacFADDEN: There is a difference in the quality immediately apparent, and there is a difference in the market charge on the two types of bonds they find themselves in.

The revenue bonds would carry a higher rate of interest than the issue behind which is the state's credit will carry. As a result, the revenue bonds tap the big investment fund reservoir of life insurance companies, and that sort of thing, which have apparently no interest in 99 percent. of the times, in general obligation bonds which sell at 1 percent. or 1½ percent.

lower in yield.

So your general obligation bonds will have to be sold to a different class of buyers, and the general approach is to a class of buyers which is not as great in its financial resources, as were approached with the revenue bonds.

In other words, it would be very difficult to sell next week $400,000,000 of Illinois bonds without dragging the price of those bonds, as general obligation bonds, down to the level at which they can be sold. You would have to bring the price down to almost a lower level, before you could approach the big investment companies.

MR. YAREMKO, Q.C.: In the investment field, is not the state of California going further than these states, because many of the states are hesitant about giving a guarantee beyond a certain limit, whereas the state of California has put all of its resources available?

MR. MacFADDEN: I would say California has adhered to the old pattern, and that is, financing all their requirements in the same manner they have done over the years past, whereas these other areas have veered into other financing.

It is no longer new. Our first toll road was

completed in 1948, so you can see it is no longer a new field.

But, in answer to your question, California has adhered to the old-line approach to the market to meet its needs. These other areas have found a way to meet those needs, by increasing the direct tax load on the taxpayers.

MR. ROOT: I wonder, Mr. MacFadden, if California has pledged the state to build the roads, how that would affect the interest rate if that state wanted to borrow for other projects.

MR. MacFADDEN: So long as they did not borrow too much. If they go to sell their bonds, and become saturated through repetition, it might be a different picture.

We have seen that in the east, in the state of Maine, where they have come repeatedly to market over all the post-war years, with the result that the investment companies are now so filled up with Maine bonds, that they do not want to, or cannot, take any more. So the state is searching for new placements, with the result that the state has increasingly had to pay more for its borrowings.

I think the same thing would apply in California, under the same conditions.

MR. ROOT: In other words, if, in Ontario, instead of building toll roads, we decided to pledge the province to build free roads, it would affect our interest rate if we went back into the money market for other purposes?

MR. MacFADDEN: If the province for another purpose went out to borrow $150 million, and the investors knew that there was a plan on the board for selling an additional $150 million guaranteed toll road bonds six months later, it might affect the rate on which the first issue would sell, and on the second.

It is a case of the old theory of coming to the well too often, and too soon.

MR. SKELLEY: . . .: Under the California system, bonds are sold on a rate basis, starting with "A", and going down, but, as Mr. Lynch has pointed out, the California credit has already declined from "triple 'A'" to "double 'A'", and so the bonds are selling on about a single "A" level, so a single "A" is possible before long.

They have imposed that burden on the entire population, but, of course, in California, as probably in Ontario and other places, where your cities are widely scattered, the automobile is necessary, so perhaps the philosophy is that everybody should pay for

the automobile roads. Perhaps that is a correct philosophy.

That is something you would have to thresh out in your own deliberations.

The amount of money put on per head of the people is the real factor. In other words, how many people are there to pay that interest, and pay the principal when it becomes due?

There is another factor which appears in connection with your large investments in the toll roads, and that is the fact that these bonds are term bonds, that is, they become due at a certain time in the future. It is a policy based on something that is coming in not next year or in five years from now, but something which is coming in in thirty years, so they will know what their returns will be. That is the appealing factor, as far as the large institutional investors are concerned.

My knowledge of the Canadian conditions is confined entirely to British Columbia, where we did some work both for the city of Vancouver, and several of the municipalities. If you must issue these bonds on a sinking fund basis, that is, where they must retire them on a regular schedule, that closes a good segment of the market now, because there would

be a small tax.

In regard to Ontario bonds, they need an insurance company who does business in Ontario, and that is another factor, as it sometimes is, in the state credit here.

For instance, I think South Carolina imposes a tax on foreign corporations, so that an insurance company doing business in South Carolina would generally not buy South Carolina bonds. But I do not think it would exist in enough volume to make it a factor.

Our business with the insurance companies,-- as a matter of fact, is the opposite, that is, that the Canadian companies buy more insurance, but nowhere in the United States investment business has the business been extended down here. There have been ample investments in Canada, which is a factor in what we call the "rate differential" between the United States buying issues and the Canadians buying issues. That factor is about one-half to three -quarters of 1 percent. in favour of the United States issues.

We are contemplating at the present time, a large piece of financing for the West Coast Transmission Line, which will bring the gas from the Peace River to the province of British Columbia, and into the United States. In that case, we have virtually

taken off the Canadian bought bonds as it calls for the U.S. bought bonds.

You would be faced with this factor, too, that you would have to have a U.S. issue. There is no question about that.

You might just as well write that down right away, because I do not think the market is large enough to take the Canadian buys, and the U.S. investors are limited by the loans to New York state, and other states, as far as foreign investments are concerned.

MR. MacFADDEN: I would like to express an opinion which may not be at all applicable in your area, but it has become pretty soundly established in a number of our states. That is, if your principal traffic arteries between your principal population centres would serve an intermediate group, the population centres can be financed on a "user-pay-the-toll" basis, which is a toll road matter. That is a great advantage.

Your province is a large one, and you have roads branching off for 100 or 125 miles in each direction, and like the state of Texas or any other large areas, those areas are always in need of additional money to build up the secondary or rural road systems.

If you can take care of your main arteries, and have them paid for directly by the users, you get the over-all rate to the taxpayers down, and you limit them to certain graded arteries, and the users of them have the advantage of being able to develop further your other road systems. I would think an accepted principle, would be well on the way toward doing that.

Where a road can be paid for and liquidated by the users, it would provide corollary advantages through the entire state or province, and to the taxpayers.

MR. LYNCH: The point about the actual cost of running these toll roads; for instance, truckers will use them because of the saving in time and distance. To them it is a saving even though they are paying the toll, so that the toll in itself is not a burden to the truckers, and the mere fact that you have a toll on the road means it will not be a burden on the taxpayers either.

THE CHAIRMAN: We find in visiting where we have up to date, that these roads, in the over-all economy of your social units, seem to be taking the place of the highways. In other words, where your road goes there goes your industry and housing, and so on, and while that is probably true, I wonder if the bankers feel they are further protecting the bonds, as far as

Ontario is concerned.

We might want to build these roads, even accepting the fact that there may not be sufficient traffic there at the present time to justify the facility. But if we build it, we are affording more benefit and help to the existing traffic, and from the point of view of inducing more traffic and more industry, which takes us well out of the classic toll picture entirely.

You mentioned one state as being a "spending state", and we may be putting on an over-all political philosophy.

MR. LYNCH: Part of that may be due to the fact that they have developed a system of economics very rapidly -- the general economy of the area. A great number of people are moving west.

MR. MacFADDEN: I think you have a very interesting point in that, and your philosophy and approach may be different than what has been accepted generally here, in which case you may find the provincial government essential to that kind of development.

THE CHAIRMAN: The present road is being constructed now as a freeway, at the rate of about 75 miles a year. It runs from Windsor on the west, to the Quebec border on the east.

We were astounded at a meeting in New Jersey yesterday when they told us their highway appropriation is $20,000,000 a year, yet with half again as many registrations, our highway budget last year was $187,000,000 so we are at present paying for roads out of current revenue.

MR. MacFADDEN: It is a heavy highway budget.

THE CHAIRMAN: We have two experts here, and they can tell you that we have vast stretches of highway which will come close to being used to capacity, but even if one person wants to use the road, it has to be there.

MR. MacFADDEN: What does it cost to build a four-lane divided road in Ontario?

MR. FULTON: We have two hundred or three hundred miles of a standard that is comparable to the toll roads, and with grade separations, interchanges, four lanes, and a median strip, it has been costing us from $600,000 to $700,000 a mile.

MR. MacFADDEN: That compares very favourably with our roads here. Our cheapest road was the one to link up with the Pennsylvania Turnpike. The next was a turnpike in Oklahoma, connecting Oklahoma City with Tulsa, and that was about $480,000 per mile, but now, most of the roads are running $1 million-plus.

MR. AULD: Would that have a good deal to do with property costs?

MR. MacFADDEN: It has a great deal to do with the property costs, and the terrain.

In the western and the Plain states, it is generally flat and rolling in contour with an avoidance of major rivers, which is a factor which boosts the over-all cost tremendously, and which the mountainous western states, and some of the eastern states have had to contend with.

MR. MacDONALD: Mention was made earlier of the fact that California is a greatly-expanding state and has done very heavy borrowing for highways, as well as different other things, and that fact is now reflected in its credit rating.

We have much the same situation in Ontario, with very heavy expenses for highways and other things, and yet we have very good credit in Ontario.

MR. MacFADDEN: I would say that yours has the premier credit of the Dominion.

MR. ROOT: Along that line, do you think that the province backing the toll bonds would offset, in the money market, the Federal taxation?

MR. MacFADDEN: It will go a long way toward that.

MR. LYNCH: I would say yes definitely, because it will attract a certain type of local investors, where a revenue bond would not be a local investment, so it would affect the interest rate favourably.

MR. ROOT: How did you offset the Federal tax?

MR. POWER: Because they were being bought by people who did not pay a great deal of Federal taxes. The yield is 30 base point between 3 point 70 and 4 point. It is about 30 base point, and if they get a tax point yielding 3 percent., it is compared with the Federal 4 percent. taxable yield.

Where the Federal tax factor enters into it, it is supported by both the institution and the individual, but more by the individual.

Some projects have been financed almost without institutional support, or with meagre institutional support, but the tax-exemption coupons appeal to the individual.

You might cite the case of the Mackinac Bridge, where an issue came in as an individual issue, where the individual can take the risk, because of the tax exemption they would have in the meantime.

MR. MacFADDEN: And a higher coupon.

MR. POWER: Each individual case has to be

looked at by itself. That is the reason, as was pointed out, that when you get to that point you should have banking advice right from the start, so you will not have to correct what you are doing at perhaps the least opportune time.

MR. LYNCH: The size of the issue can have a great deal to do with what you will have to pay in the way of rate. In regard to the New York Thruway, there were both revenue bonds and guaranteed bonds, but the difference there is under 1 percent. It is a much narrower spread.

MR. COLLINS (Secretary): But the revenue bonds there have a prior lien?

MR. LYNCH: That is right. If your bond is good enough, it will make up the difference.

MR. MacDONALD: Would you elaborate on this "safety factor". As I recollect, some of the Authorities said it had to be in your original estimate of 80 percent. margin between the revenue required to carry the thing, and what they estimated might be coming in. Is that normal?

THE CHAIRMAN: I think that is a Thruway figure.

MR. MacDONALD: Perhaps.

MR. MacFADDEN: Yes, that is a Thruway figure.

I would, at this point, approach it a little differently. Mr. Robarts mentioned that was the Thruway approach. I would say that a toll road in an area like this, to successfully come to market, would have a coverage of debt, after operating and maintenance requirements, of course, of about one and one-half times, plus or minus a little.

MR. LYNCH: That is interest cost?

MR. MacDONALD: In other words, a 50 percent. margin beyond what is required?

MR. MacFADDEN: Yes. There has been, and will be, financing in this country with a lower requirement, but this will be a pioneering effort, the first in your country, in an area where this type of financing has not an established background.

You would be -- I do not like to say "penalized"-- but there would be extra safety requirements required in the eyes of the United States investors, because of those points.

MR. ROOT: Something was said a while ago about tolls could be lowered if the bonds were backed by the state or province?

MR. MacFADDEN: Yes.

MR. ROOT: Does the state, in its backing, help set the toll?

MR. MacFADDEN: I would think they would have a good deal to say about it. Your toll would be set in consultation with your engineer, but here the state has a direct finger in everything, and they have a very great voice in what happens. I think it would be quite comparable in the province of Ontario, that the province would exert their thinking in that same situation, at least, to some degree.

On the other hand, I do not know, but they might adopt an entirely "hands off" policy, and leave it in the hands of the governing group of such a toll road.

MR. LYNCH: The large investors -- which may be some of the large insurance companies -- may dictate pretty much the manner in which tolls would be charged.

MR. YAREMKO, Q.C.: Does that enter into the safety factor? If a toll produced a safety factor, of 2.5, you could bring it down to 1.50 --

MR. MacFADDEN: And, conversely, no toll will be pushed up to the point where diminishing returns set in. So it works both ways.

Inbetween, there is a mean, which is sound and economically fair and usable, and that is what we are attempting to achieve.

MR. LYNCH: There will be rate covenant in

the indenture, which will require a realistic approach, and which may require something additional, even though the bonds are marketed.

MR. ROOT: Who appoints the Authority?

MR. MacFADDEN: In most of our states, they are appointed by the Governor, usually for rotating terms, so there is a continuity in the main body, but new members are injected over the years.

MR. ROOT: The investor has no power to appoint anybody?

MR. MacFADDEN: No, and should not. It is up to the state or province.

MR. MacDONALD: Coming back to the safety factor again; what safety factor would be permitted, if the government amortized the bonds?

MR. MacFADDEN: With a provincial guarantee, you could go to 1.1, or you might even go below that. It does not matter, because the credit of Ontario would be behind them, and the investors would look to the province of Ontario for payment of the bonds.

You might cover the earned revenue, or you might improve it by a wide margin.

MR. MacDONALD: The 1.5 which you mentioned --

MR. MacFADDEN: Was on a self-sustaining revenue basis.

THE CHAIRMAN: And the higher the percentage, the sooner you pay the bonds off.

MR. MacFADDEN: In that connection, it is very interesting to observe that in almost all of the toll roads we have in successful operation, it has been successful theoretically long before maturity, but there again we run into the economic factor, that those rates will be --

THE CHAIRMAN: It turns out to be a very painless way for a political body to build new roads. I do not think we have seen the end of it, and none of them will fold up after the bonds are paid for.

MR. MacDONALD: I notice you use the word "successful" in connection with toll roads, before their bonds have matured. Are there any others?

MR. MacFADDEN: There is one which we questioned. That is the one in Virginia. It is built over rugged terrain, which is really rough. They initially came out with a $600-million bond issue, and had to come to market again for another loan. That created a load which was never contemplated. The engineers "missed the boat". The road will ultimately be a good road, but right now revenues are well below expectations and will probably continue so for a few years. As it stands there now, they are attempting

to secure additional traffic, or something of that sort.

MR. JAMIESON: What is the normal term of the bonds?

MR. MacFADDEN: 40 years.

MR. POWER: I would like to qualify one of my statements, when I said a "term bond". That does not mean it is not paid out, but it is the length of the pay-out that is concerning the insurance companies, because they are selling that which can only come out forty years from now.

MR. MacFADDEN: Where most of our financing has been done on a forty-year term, there is a sinking fund which becomes operative after the first few years, which immediately affects the reducing action of the total bonds, and that accelerates as the years progress.

So I would guess -- and it is only a guess -- that the average good toll road, if financed on a forty-year term-bond basis will pay out in about twenty-five or twenty-eight years. It may be sooner in some cases, but I think that would be a fair presumption of the anticipated performance.

MR. LYNCH: I might point out that the actual cost to the province or the state is the amount of money which will be spent over the life of the bonds to pay for their retirement and for the interest.

Now, the revenue bond has a much higher coverage, as you have been pointing out. That makes possible the prior retirement of that bond, and it will always work out. If the retirement is carried on, the actual cost to the people will be less than under current arrangements, because there the chances of prior retirements are rather small.

So they run for forty years, and the total interest over a forty-year period is very high.

MR. MacFADDEN: That is very true.

MR. WELDON: There is one question on the current issue. Would it have any effect on the highway financing in Ontario?

MR. MacDONALD: It would have some influence.

MR. WELDON: It is bound to have some effect.

MR. MacFADDEN: I think we might adjourn now, Mr. Chairman. Luncheon is being arranged in the Club just across the way on Wall Street.

THE CHAIRMAN: Very well, Mr. MacFadden.

---Whereupon a short recess was had.

---The Committee reconvened at a luncheon tendered by Messrs. Eastman, Dillon and Company, in the Wall Street Club, New York City, Wednesday, October 19th, 1955 at 12:30 o'clock p.m.

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MR. ROBARTS, Q.C. (Chairman): Mr. Gelmour and gentlemen; I would like, on behalf of our Committee, to say a very sincere "thank you" for your hospitality, and also for the information we have secured from members of your firm this morning, particularly Mr. MacFadden, Mr. Lynch and Mr. Power.

I thought, when we were listening to Mr. MacFadden present what we consider to be a very complicated subject,in such a very simple manner -- I thought to myself, "There is a true expert". It is like watching "Ben" Hogan playing golf, you say to yourself, "I could do that; it is only necessary to take a golf club and stand up to the tee".

You have opened our eyes, and have filled in a number of gaps in our information, and we are very grateful to you, and we thank you very much.

MR. POWER: If there are further questions, I am sure Mr. MacFadden and Mr. Lynch would be happy to stay as long as you wish, with you.

We have enjoyed having you here, and we hope you will come back to us for some further information, and that some day we may be marching hand-in-hand to bring this to the investing public.

I thank you very much.

I presume the meeting can now stand adjourned,